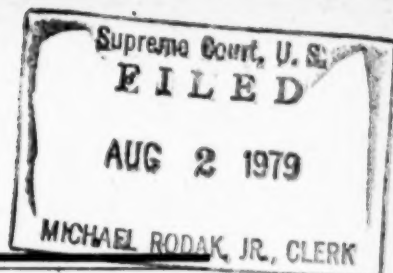


No. 78-1915



In the Supreme Court of the United States

OCTOBER TERM, 1978

YAFFE IRON & METAL CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

**ON PETITION FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR
THE EIGHTH CIRCUIT**

**MEMORANDUM FOR THE UNITED STATES
IN OPPOSITION**

WADE H. MCCREE, JR.
Solicitor General
Department of Justice
Washington, D.C. 20530

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The sole question presented in this federal income tax case is whether the decision below correctly held that petitioner and another corporation constituted a "controlled group of corporations" within the meaning of Section 1563(a)(2) of the Internal Revenue Code of 1954 (26 U.S.C.), and were therefore entitled to only one corporate surtax exemption.

Section 1561 of the Code denies to members of a controlled group of corporations more than one surtax exemption. Section 1563(a)(2) defines "controlled group of corporations" to include two or more corporations if five or fewer individuals own stock possessing (A) at least 80 percent of the combined voting power or of the total value of the stock of each corporation, and (B) more than 50 percent of the combined voting power or total value of

the stock of each corporation, taking into account for this latter purpose stock ownership of an individual only to the extent of that individual's identical ownership with respect to each corporation (Pet. App. 12, 13). Finally, Section 1563(d)(2) provides that, for purposes of determining whether a corporation is a member of a controlled group of corporations, stock owned by an individual means stock owned directly plus stock owned indirectly under the constructive ownership rules set forth in Section 1563(e). Under these rules, stock owned by a corporation is deemed to be owned by its shareholders in proportion to the value of their stock interest in such corporation. See Section 1563(e)(4).

Here, three shareholders owned all of petitioner's stock. Two of the shareholders were individuals—Richard Yaffee, who owned 30 percent of such stock, and Robert Yaffe, who owned 32.5 percent. The third shareholder, Yaffe-Muskogee, a corporation, owned the remaining 37.5 percent. Robert Yaffe in turn owned 51 percent of Yaffe-Muskogee (Pet. App. 12, 13). Applying the constructive ownership rules of Section 1563(e)(4), the Commissioner attributed to the shareholders of Yaffe-Muskogee the 37.5 percent interest held by that corporation in petitioner. He then determined that the requisite degree of common ownership existed (*i.e.*, that the 80-percent and 50-percent tests set forth in Section 1563(a)(2) were satisfied) and hence concluded that the two corporations formed a brother-sister controlled group (Pet. App. 22-23).

In this refund suit brought by petitioner in the United States District Court for the Western District of Arkansas, the district court upheld the Commissioner's position that petitioner and Yaffe-Muskogee were a controlled group pursuant to Section 1563 (Pet. App. 11-17). The court of appeals affirmed (Pet. App. 19-26).

Petitioner argues that (Pet. 9-10) in concluding that Robert Yaffe owned more than 50 percent of its stock and that of Yaffe-Muskogee, the decision below misapplied the 50-percent test of Section 1563.¹ In petitioner's view, the stock constructively owned by Robert Yaffe should not have been taken into account in applying the 50-percent test because such constructively owned stock is not "identical" to directly owned stock.² In support of its argument, petitioner relies on the statutory language that each individual's stock interest is to be considered "only to the extent such stock ownership is identical with respect to each such corporation."

But as the court of appeals pointed out in rejecting the same argument (Pet. App. 24), Section 1563(f)(2) specifically provides that stock constructively owned by a person (by reason of the application of attribution rules contained in Section 1563(e)) shall "be treated as actually owned by such person." Accordingly, it is apparent that

¹Robert Yaffe owned directly 32.5 percent of petitioner's stock and 51 percent of the stock of Yaffe-Muskogee. Since Yaffe-Muskogee in turn owned 37.5 percent of petitioner's stock, the courts below, applying the stock attribution rules of Section 1563(e)(4), determined that Robert Yaffe constructively owned an additional 19.125 percent (51 percent x 37.5 percent) of petitioner's stock thereby attributing to him a total of 51.625 percent of the stock (Pet. App. 15; Pet. App. 23-24).

²Although petitioner contended below that neither the 80-percent nor the 50-percent test was satisfied, it now challenges only the determination that the 50-percent test was satisfied.

the courts below correctly held that the 50-percent test of common ownership was satisfied.³

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. MCCREE, JR.
Solicitor General

AUGUST 1979

³Petitioner is equally mistaken in asserting (Pet. 7, 9) that the decision below renders the 50-percent test superfluous because that test necessarily will be met whenever the 80-percent test has been satisfied. Unlike the 80-percent test, the 50-percent test requires that each person whose holdings are considered in applying the test must own stock, actually or constructively, in each of the controlled corporations. See *T.L. Hunt, Inc. v. Commissioner*, 562 F. 2d 532 (8th Cir. 1977); *Fairfax Auto Parts, Inc. v. Commissioner*, 548 F. 2d 501 (4th Cir.), cert. denied, 434 U.S. 904 (1977). The decision below in no way impairs this distinction between the two tests.